

# **HTSUS 9802.00.60 – Metal Articles Previously Exported for Processing Pre-Assessment Survey**

## **Internal Control Technical Guide**

### **Objective**

Provide guidance for performing a Pre-Assessment Survey (PAS) of the company's internal control for merchandise entered under HTSUS 9802.00.60 and evaluating the results.

### **Background**

Generally Accepted Government Auditing Standards require the PAS team to obtain a sufficient understanding of internal control to plan the audit and determine the nature, timing, and extent of tests to be performed.

The guidelines and terms in this technical guide are based on *Assessing Internal Controls in Performance Audits*, GAO/OP-4.1.4, published by the United States General Accounting Office, Office of Policy, September 1990; and American Institute of Certified Public Accountants *Statement on Auditing Standards No. 78*.

9802.00.60 constitutes any article of metal (except precious metals) manufactured in the U.S. or subjected to a process of manufacture in the U.S. and exported for further processing, and any article of metal which results from processing outside the U.S. and is then returned to the U.S. for further processing. The returned articles are dutiable on the value of the processing outside the U.S., provided the documentary requirements of 19 CFR 10.9 are met.

Title 19 CFR 10.9 states: "Except as otherwise provided for in this section, the following documents shall be filed in connection with the entry of articles which are returned after having been exported for further processing and which are claimed to be subject to duty only on the value of the processing performed abroad under subheading 9802.00.60, Harmonized Tariff Schedule of the United States (HTSUS): (1) A declaration from the person who performed the processing abroad....; and (2) A declaration by the owner, importer, consignee, or agent having knowledge of the pertinent facts...."

HTSUS 9802.00.60 imposes a dual "further processing" requirement on qualifying metal articles: foreign processing, and when returned, domestic processing. More specifically, "further" processing refers to processing that changes the shape of the metal or imparts new and different characteristics, which become an integral part of the metal itself and which did not exist in the metal before processing. Thus, further processing includes machining, grinding, drilling, threading, punching, forming, plating, and the like, but does not include painting or the mere assembly of finished parts by bolting, welding, etc."

### **Examples of Red Flags**

The following examples are conditions, which may indicate a potential problem in 9802.00.60.

- Company has insufficiently documented, poorly defined, or no internal control for accurately declaring 9802.00.60 for Customs purposes. Examples:
  - ✓ Company does not monitor or interact with the broker on 9802.00.60 issues.

- ✓ Company relies on one employee to handle 9802.00.60 issues, and there are poor or no management checks or balances over this employee.
- Company Customs staff lacks knowledge of 9802.00.60 eligibility requirements.
- Company's import staff lacks the knowledge of cost accounting that is necessary to determine whether the value covers all costs and profit for processing performed by related parties and to ensure that supporting cost records are retained and readily available.
- Company offers unreasonable explanations to Customs.
- Company fails to cooperate with or respond to Customs.
- Company has high turnover of people in key positions.
- A significant variance exists between the importer's data and Customs data.
- Customs (import specialist, account manager, compliance measurement, prior audit) shows history of problems with 9802.00.60.
- The Questionnaire indicated that the company does not have procedures to:
  - ✓ Verify processor's declarations (see reasonable care – United States v. Golden Ship Trading Company, Joanne Wu and American Motorists Insurance Company, Slip Op. 01-7).
  - ✓ Review processing operations performed at the foreign plant to determine whether such operations qualify as further processing (i.e., not just assembly).
  - ✓ Establish that further processing in the U.S. occurred.
  - ✓ Verify that the imported articles are the same as the exported articles.
- Company has many drawback claims.
- Article doesn't receive further processing before sale.
- The product goes directly to finished goods inventory.
- Importer and foreign processing sites are related and all elements of cost and profit, including overhead, general expenses and profit, are not included in the processing value. Foreign processing is often performed by the related foreign factories that manufactured the products. Transaction value may not be acceptable if the processing value does not cover all costs and a reasonable profit.

### Examples of Best Practices

- Internal controls over 9802.00.60:
  - ✓ Are in writing;
  - ✓ Include procedures for monitoring and feedback; and
  - ✓ Are monitored by management.
- One manager is ultimately responsible for control of the Import Department, including ensuring eligibility of merchandise entered under 9802.00.60. That manager has knowledge of Customs matters and the authority to ensure that internal control procedures for imports are established and followed by all company departments.
- The Import Manager also has cost accounting knowledge, for control of imports from related parties.
- Written internal control procedures assign 9802.00.60 related duties and tasks to a position rather than a person.
- Company has good interdepartmental communication about 9802.00.60 matters.
- Company conducts and documents periodic reviews of 9802.00.60 merchandise, and uses the results to make corrections past and present to entries and changes to their import operations as appropriate.

- The importer or the importer's agent visits the plant in the country where the 9802.00.60 products are processed.

### Examples of Documents and Information to Review

- Internal control policies and procedures for ensuring proper handling of 9802.00.60.
- The company's response to the questionnaire.
- Interviews with company staff concerning actual procedures and controls specific to 9802.00.60.
- Company's documentation that supports monitoring and verification of established and/or written internal control for 9802.00.60, such as:
  - ✓ Processor's Declarations;
  - ✓ Importer's Declarations;
  - ✓ Entry documents (CF 7501, invoice, etc.);
  - ✓ Export documents (invoices, bills of lading, etc.);
  - ✓ Bills of material and/or detailed breakdown of standard material costs;
  - ✓ Processing orders and contract documenting the reason of exportation; and
  - ✓ Production records.
  - ✓ Cost sheets from related parties performing processing and allocation worksheets for overhead, general expenses, and profit.
- Internal and external audit reports.

### Suggested Testing

PAS team judgment should be used to determine the type and amount of testing needed to evaluate how effective internal control is and whether there is sufficient risk to warrant proceeding to the Assessment Compliance Testing (ACT) process.

Using the chart and guidelines below, determine through limited judgmental testing whether the company's internal control is effective.

To determine the extensiveness of internal control testing, it is necessary to evaluate:

1. The **risk exposure**, and
2. The **internal control** system by determining if the controls are in operation, how the controls were applied, how consistently they were applied, and who applied them.

### Risk Exposure

Risk exposure is the probability of significant Customs noncompliance. In each step of determining risk exposure, consideration should be given to:

1. Significance (to Customs) and sensitivity (e.g., issues of interest to Congress or the media, or impacting admissibility).
2. Susceptibility (of making incorrect declarations).
3. The existence of any "red flags."
4. Management support (of strong internal control).

5. Competent personnel (to adequately administer the controls).

*Steps to Determine Risk Exposure:*

1. Evaluate problems identified in the profile, compliance measurement rates, questionnaire, concerns raised by the import specialist and account manager.
2. Perform the macro risk analysis tests.
3. Analyze the macro risk analysis tests to determine the risk exposure level.
4. Evaluation of the risk exposure is not simply a one-time process that occurs at the start of the PAS process. Continually reassess risk exposure as more information is gathered from evaluating internal control and performing other work in the PAS

**Macro Risk Analysis Examples**

*Example A: Low Risk Exposure*

The CAS found that the amounts paid to the foreign processor closely matched amounts in ACS, and the quantity reported as 9802.00.60 in ACS also closely matched quantity recorded in the company records. The profile identified no risk associated with 9802.00.60, and the import specialist and account manager did not have any concerns on this area. Therefore, the macro risk analyses indicated low risk exposure.

*Example B: High Risk Exposure*

The CAS verified that the amounts paid to the foreign processor closely matched ACS, the profile identified no risk associated with 9802.00.60, and discussions with the import specialist and account manager disclosed no concerns with 9802.00.60. However, when the PAS team compared the quantities of exported articles to imported articles, it determined that the materials imported exceeded quantities of material originally exported. Therefore, the macro risk analyses indicated a high risk exposure.

**System of Internal Control**

To evaluate the internal control system:

1. Consider the five components of internal control:
  - Control Environment.
  - Risk Assessment.
  - Control Activities.
  - Information and Communication.
  - Monitoring.
2. Review relevant Customs and company documents to identify and understand relevant internal control over 9802.00.60 entries. (Examples of documents and information to review are listed on the prior page.)

3. Determine whether the company has established and follows procedures. Review:
  - Documentary evidence of the results of periodic internal control reviews/testing and corrective action implemented.
  - Documentary evidence (such as a log) of communication with the broker and company departments on 9802.00.60 issues, including company testing of broker operations and verification that the broker followed company instructions.
  - Documentary evidence that company-specific rulings are requested and followed.
  - Documentary evidence of intra-company communications to ensure correct information is provided to Customs.
  - Training records and materials relating to 9802.00.60 used to educate staff on Customs matters.
  - Documentary evidence that the company ensures the merchandise was exported from the U.S. without payment of drawback.
  - Documentary evidence (such as certificates of origin or manufacturer's affidavits) that demonstrate that the company ensured that metal articles exported from the U.S. have been manufactured in the U.S. or, if of foreign origin, were subjected to a process of manufacture in the U.S. before being exported for further processing.
  - Documentary evidence that the company ensures that articles imported in their processed condition are the same articles that were exported.
  - Documentary evidence, such as engineering drawings, showing that the company ensured the processes performed in foreign country and U.S. are considered further processing.
4. Review written policies and procedures and interview applicable company personnel to complete appropriate sections of the "Worksheet for Evaluating Internal Control Over 9802.00.60."

Note: The internal control assessment should include steps to:

- Identify and understand internal control
- Determine what is already known about control effectiveness
- Assess the adequacy of internal control design
- Determine whether controls are implemented and effective
- Determine whether transaction processes are documented

### **Extensiveness of Audit Tests (Testing Limits)**

The purpose of limited PAS testing is to take a survey in order to determine the necessity for and extent of substantive tests. In some circumstances, the PAS team may decide that it probably will not be able to form an opinion based on limited PAS testing. In that case, it may be necessary to proceed immediately to the ACT process. If the PAS team believes that it can form an opinion based on limited PAS testing, it should test the appropriate number of controls and associated transactions using the table below. Tests may be appropriate for various areas below the overall 9802 level that will be reported on. For example, the company may import from various foreign entities and from various countries and tests may be designed for areas identified as the primary risks.

### **Determine Extensiveness of Audit Tests**

<b>Risk Exposure</b>	<b>+</b>	<b>Preliminary Review Internal Control</b>	<b>=</b>	<b>Extensiveness of Audit Test</b>	<b>Testing Limit</b>
<b>High</b>		Weak Adequate Strong		High Moderate to High Low to Moderate	10-20
<b>Moderate</b>		Weak Adequate Strong		Moderate to High Moderate Low	5-15
<b>Low</b>		Weak Adequate Strong		Low to Moderate Low Very Low	1-10

Source: Adapted from *Assessing Internal Controls in Performance Audits*.  
Column titled "Testing Limit" reflects Customs test sizes.

**Note:**

PAS audit tests for 9802.00.60 should be used to confirm that internal control is reasonably adequate to assure that 9802.00.60 claims are accurately declared.

*Example: Validation of Company Control Activity*

One of the company's internal controls over 9802.00.60 is that they review every 20<sup>th</sup> 9802.00.60 transaction to ensure that 9802.00.60 are properly declared. The company maintains a "9802.00.60 Review Log" to document this review process. To determine internal control effectiveness, the PAS team may decide to verify that the company review procedure identifies incorrectly declared 9802.00.60 and the company takes appropriate corrective action, including improved procedures to avoid future improperly declared 9802.00.60.

The PAS team may select a limited number of reviewed items from the "9802.00.60 Review Log" to verify that 9802.00.60 was adequately reviewed to determine accurate declaration of 9802.00.60, and that any incorrectly declared 9802.00.60 entries were corrected (causes identified and procedures corrected to ensure future compliance) and reported to Customs.

In addition, the PAS team should verify that the company took action to avoid future improperly declared 9802.00.60 after such errors were identified. In order to do this, the PAS team should verify that the same types of improperly declared items were correctly declared on subsequent entries. Following are examples of some of the tests that can be performed to determine if 9802.00.60 is accurately declared:

- Review processor's and importer's declarations to verify documentary requirements of 19 CFR 10.9 are met.
- Trace the imported articles through receiving and inventory records into work in process to verify further processing was performed in the U.S.
- Determine types of records (i.e., general ledger accounts, management reports, production reports, etc.) used by importer to determine costs of material, labor, overhead, general and administrative expenses and profit, and cost or value of the

processing actually performed abroad and have importer demonstrate how entry information was developed.

## Evaluation of Pre-Assessment Survey Testing Results

The following steps are guidance for determining the effectiveness of company's internal control over 9802.00.60.

1. Complete the "Worksheet for Evaluating Internal Control Over 9802.00.60" to determine whether risk determination is acceptable or unacceptable and to document why. Put results of testing in perspective and evaluate confirmed weakness as a whole. The evaluation should consider the results of the internal control testing, problems identified in the profile, and/or concerns raised by the import specialist or account manager. The team must evaluate the PAS results based on the specific situations.

Customs considers risk to be unacceptable when testing reveals that internal control is not sufficient or effective in providing reasonable assurance that accurate, timely, and complete declarations are reported to Customs.

2. The following will assist the PAS team in determining whether conditions warrant proceeding to ACT.

- **Do not proceed to ACT (Revenue) if:**

- ✓ Cost benefit analysis warranted no further effort (do not spend a significant amount of resources to identify a potential loss of revenue considered insignificant).
- ✓ The PAS indicated that the revenue loss was due to an isolated incident.
- ✓ The company agreed with the PAS finding(s) and agrees to quantify actual loss of revenue within an acceptable time frame.

- **Do not proceed to ACT (Compliance) if:**

- ✓ Error was isolated and the importer can show identical entry lines are correct.
- ✓ Errors were systemic but the importer agreed to develop and implement a Compliance Improvement Plan within an acceptable time frame.

- **Proceed to ACT (Revenue) if:**

- ✓ Company does not have adequate internal control and PAS indicated material loss of revenue that cannot be quantified without statistical sampling or further review.
- ✓ Importer will not quantify loss of revenue.

- **Proceed to ACT (Compliance) if:**

- ✓ The company refuses to take corrective action on systemic errors, and it is necessary to calculate a compliance rate.

Note: If substantive tests necessary to determine a compliance rate or revenue loss can be quickly performed without extensive effort, the team should immediately perform the substantive tests without proceeding to ACT.

3. Determine whether referrals should be made for enforcement action.

## Examples

The following examples of situations that might be encountered under PAS *are for clarification only*.

*Example A: Situation in which the team would not proceed to ACT (Revenue)*

Company's Policies and Procedures

The company's Customs Compliance Manual (CCM) requires the purchasing department to obtain a declaration from the foreign company performing the processing. The buyer submits the declaration to company's Import Department and provides assistance to the Import Department, if necessary, in preparing the Importer's Declaration. The Import Department in turn is responsible for submitting these declarations to the Customs broker with instructions to include them with the entry. The buyer is also responsible for conferring with the foreign company to make sure that the invoice to be sent to the company sets forth the processing performed and the cost or value of the processing. The production department is required to submit to the Customs Department production records documenting that the metals have been further processed in the U.S. after importation. The CCM further requires the Customs Department to maintain and have ready for submission the foreign customs entry, foreign customs invoice, and bill of lading/air waybill related to the export of the merchandise from the U.S. for processing in case the U.S. Customs Service should request additional supporting documentation.

Monitoring Activities

The CCM also established procedures to verify compliance. First, the company's Customs Department conducts a cursory review of all entries filed by the Customs broker. If an error is identified the Company sends the broker a letter describing the type of error with instructions to correct the error. In addition, the company reconciles quantities of exported articles to imported articles on a monthly basis to ensure that materials imported do not exceed quantities of materials originally exported.

Finally, the CCM establishes procedures for conducting internal audits on a semi-annual basis. The Manual requires the Import/Export Compliance Manager to select 26 entries (one from each week in the six-month period) for detailed review. If the review discloses any entry to be substantially not compliant, the Manager also checks entries made in the 15 days prior and 15 days after the non-compliant entry was made. Within two weeks of completing the audit, the Manager is required to prepare a report with findings and recommendations and submit it to the Director of the Import/Export Department.

Pre-Assessment Survey

To determine if the controls were working, the team:

- Interviewed employees in the Purchasing Department to determine if they were familiar with the procedures established in the CCM.
- Selected 5 entries from ACS and:
  - ✓ Determined if the company had the Processor's and Importer's declarations on file.
  - ✓ Reviewed processing orders to determine the type of work to be conducted by the foreign company.
  - ✓ Reviewed production records to determine the types of further processing performed in the U.S.
  - ✓ Determined whether the invoice identified the processing performed on the merchandise and the cost of the processing.
  - ✓ Compared the processing orders to the commercial invoices.



- ✓ Determined if the company maintained copies of the foreign customs entry, foreign customs invoice, bill of lading or airway bill.
- Correspondence file to the Customs brokers.
- Reviewed the most current compliance report prepared by the Import/Export Compliance Manager.

The PAS team determined that the company failed to prepare and maintain processor's declarations, failed to maintain production records verifying that further processing occurred in the U.S. after importation, and stopped conducting the semiannual compliance reviews. However, the company agrees with the PAS findings, agrees to implement corrections, and is able to quantify the actual loss of revenue caused by not being able to support 9802.00.60 eligibility. Therefore, proceeding to ACT was not considered necessary.

*Example B: Situation in which the team would not proceed to ACT (Compliance)*

The same circumstances as Example A above, except the PAS team was able to verify that controls were in place and working effectively. Proceeding to ACT was not necessary.

*Example C: Situation in which the team would proceed to ACT (Revenue)*

The same circumstances as Example A above, except the company is not able to quantify the loss of revenue caused by not being able to support 9802.00.60 eligibility. Therefore, proceeding to ACT was necessary.

*Example D: Situation where the team would proceed to ACT (Compliance)*

The same circumstances as Example A above, except the company did not agree to implement corrections and the extent of the noncompliance cannot be determined without substantive testing.

### Worksheet for Evaluating Internal Control Over 9802.00.60

Objective: Determine if the company has procedures designed to effectively control Customs risks related to 9802.00.60.

**Risk Determination:**

**Acceptable** \_\_\_\_\_

**Unacceptable** \_\_\_\_\_

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Are internal controls over 9802.00.60 formally documented?						
Are written policies and procedures approved by management?						
Are written policies and procedures reviewed and updated periodically?						
Is one manager ultimately responsible for control of the import department, including 9802.00.60?						
Does the individual overseeing compliance possess adequate cost accounting knowledge, if products are processed by related vendors?						
Does that manager have knowledge of Customs matters and the authority to assure internal control procedures for imports are established and followed by all company departments?						

<b>Internal Control</b>	<b>Yes</b>	<b>No</b>	<b>Not Applicable</b>	<b>Internal Control Manual Page Number</b>	<b>Work Paper Reference</b>	<b>Comments</b>
Do written internal control procedures assign 9802.00.60 duties and tasks to a position rather than a person?						
Does company have good interdepartmental communication about 9802.00.60 matters? Is there a reliable communication system in place to ensure employees have access to current 9802.00.60 and other Customs information? (such as rulings)?						
Does the company conduct and document periodic reviews of entries declared under 9802.00.60?						
Does the company use 9802.00.60 periodic review results to make 9802.00.60 corrections to past and presently filed entries?						
Does the company use 9802.00.60 periodic reviews to make changes to their import operations as appropriate?						
Does the company provide adequate training for employees responsible for 9802.00.60 matters?						
Does the company's recordkeeping system include a retention program and identify documents needed to support 9802.00.60 claims?						

<b>Internal Control</b>	<b>Yes</b>	<b>No</b>	<b>Not Applicable</b>	<b>Internal Control Manual Page Number</b>	<b>Work Paper Reference</b>	<b>Comments</b>
Has the company established a reliable system or procedure to produce any required entry documentation and supporting information relating to 9802.00.60?						
Does the company have procedures to ensure that merchandise imported was the same as the merchandise exported?						
Does the company have procedures in place to ensure further processing in foreign country and U.S.?						
Does the company have procedures in place to ensure that the true costs for material, labor, overhead, overhead, general expenses and profit were included in the cost of processing performed by related parties?						
Does the company have procedures in place to ensure that drawback was not previously claimed on articles entered under 9802.00.60?						
<b>Internal Control Conclusions</b>						
Does the company provide adequate broker oversight to ensure proper 9802.00.60 declarations and data accuracy?						

Internal Control	Yes	No	Not Applicable	Internal Control Manual Page Number	Work Paper Reference	Comments
Does PAS testing verify control procedures were being performed?						
Do interviews with responsible persons support control procedures?						
Does the company have adequate internal control to address specific issues identified in the profile?						
<b>List company-specific procedures and controls below (if applicable)</b>						